

DATE: September 21, 2001

TO: Brett Dahl, Administrator

FROM: Kristie Rhodes, Risk Finance Specialist

RE: 2000 Cost of Risk/Benchmark Analysis

The 2000 Cost of Risk Benchmark Analysis is complete. The 2000 RIMS Benchmark Survey is the third study conducted by Ernst & Young LLP, one of the world's leading professional services organizations for RIMS (The Risk and Insurance Management Society, Inc.), a not-for-profit organization dedicated to advancing the practice of risk management.

The 2000 survey was completed by 779 respondents, 719 of which were U.S. based, 60 Canadian. 59 of the respondents were government entities, against which RMTD is measured in this analysis. Compared with all survey respondents, government entities ranked below the average in payroll size, property values, and the number of full-time employees. Revenue size could not be compared with that of other industries because respondents used a net operating budget as their primary exposure base. Most of the larger respondents in the government group (defined as those with operating budgets greater than \$1 billion) are state governments, large cities, and very large counties. The State of Montana falls into this category with an operating budget of over \$3 billion.

The total cost of risk and composition of the cost of risk dollar statistics presented in this report, as well as the data displayed in charts and graphs were obtained from the 2000 RIMS Benchmark Survey, RMTD FY2000 SABHRS reports, Office of Budget and Program Planning and the State Fund. This benchmark schedule compares Montana to other governmental respondents and uses the governmental industry median numbers presented in the survey.

#### Total Cost of Risk

The total cost of risk in the survey is measured by the sum of:

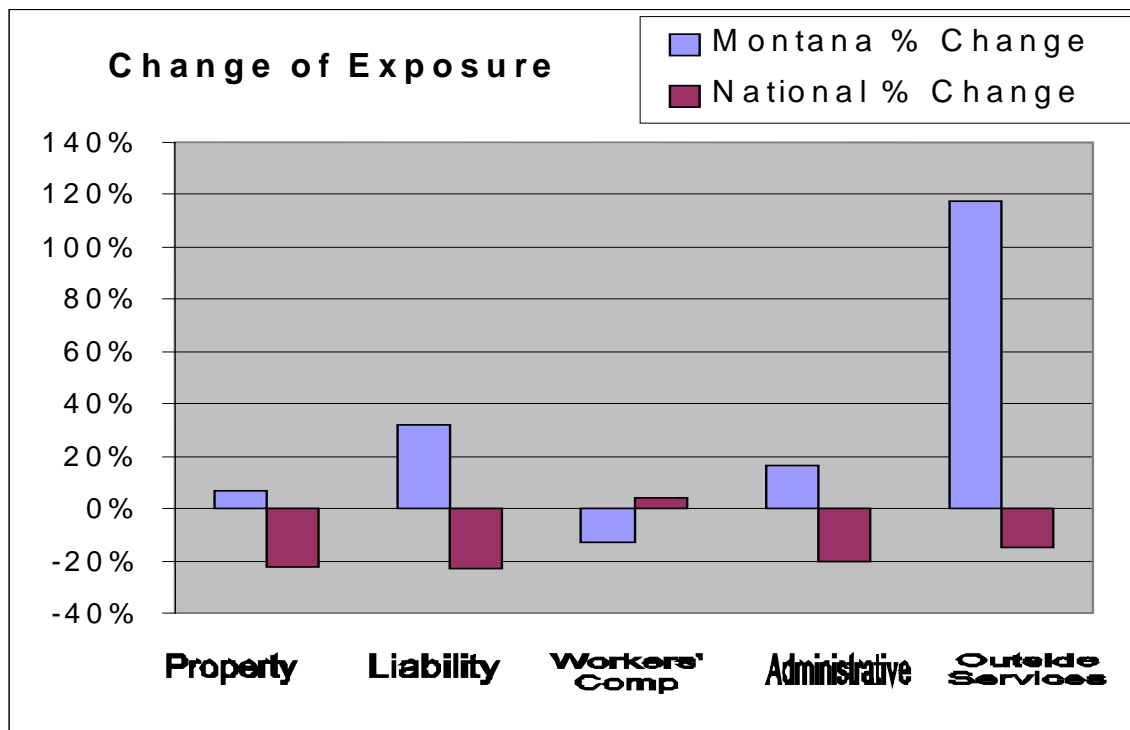
- 1) Insurance premiums for liability, property, and workers' compensation;
- 2) Retained/uninsured losses for liability, property and workers' compensation;
- 3) Risk management/insurance department administrative budgets; and
- 4) Costs for outside services such as actuarial fees.

The term "cost of risk" refers to all costs associated with an organization's risk management functions-namely, net insurance premiums, retained losses, risk control, and loss prevention expenses, and administrative costs.

Nationally, the cost of risk for all respondents decreased slightly in 2000, however government entities did not follow the decreasing trend. Government entities experienced a significant increase from the previous year, which was a result of higher workers' compensation costs. Following the government entity trend, Montana's total cost of risk increased 8% from 1999. Montana's total cost of risk in FY1999 was \$13,679,382 and \$14,809,089 in FY2000. The main factor contributing to the increase is a \$1,654,605, or 32% increase in liability costs. There was also a significant increase in outside services due to increases in actuarial, appraisal, and adjuster services. The schedule below illustrates changes by exposure for Montana's total cost of risk.

<b>Exposure</b>	<b>FY1999</b>	<b>FY2000</b>	<b>Change</b>	<b>Montana % Change</b>	<b>National % Change</b>
Property	\$1,482,911	\$1,586,407	\$103,496	7%	-22%
Liability	\$5,132,077	\$6,786,682	\$1,654,605	32%	-23%
Workers' Comp	\$6,344,490	\$5,540,818	(\$803,672)	-13%	4%
Administrative	\$662,234	\$769,873	\$107,639	16%	-20%
Outside Service	\$57,670	\$125,309	\$67,639	117%	-15%
<b>Totals</b>	<b>\$13,679,382</b>	<b>\$14,809,089</b>	<b>\$1,129,707</b>	<b>8%</b>	

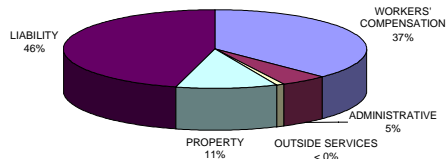
The survey shows that for all respondents nationally, the only increase was in workers' compensation costs. Montana's cost, like other government entities, did not follow the national trend in any exposure by increasing in all areas except workers' compensation costs. See the comparison graph below.



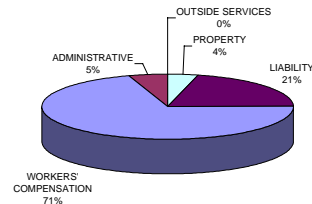
## Composition of the Cost of Risk Dollar

The composition of the cost of risk dollar shows what percentage of each risk dollar is spent on each type of exposure. The following pie charts and bar graph compare the State of Montana to other governmental entities participating in the survey.

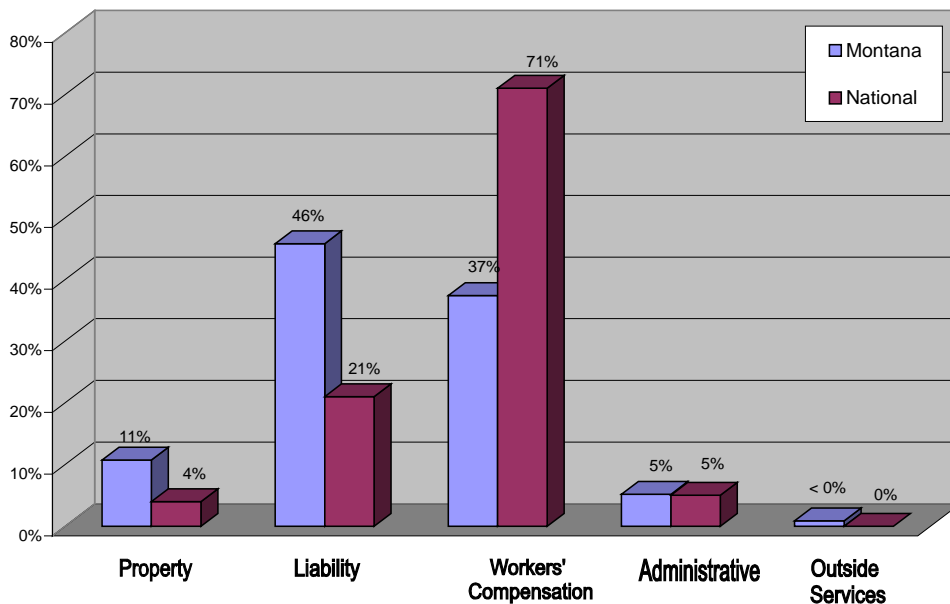
Montana Composition of Cost of Risk Dollar



National Composition of Cost of Risk Dollar



## Composition of Cost of Risk Dollar

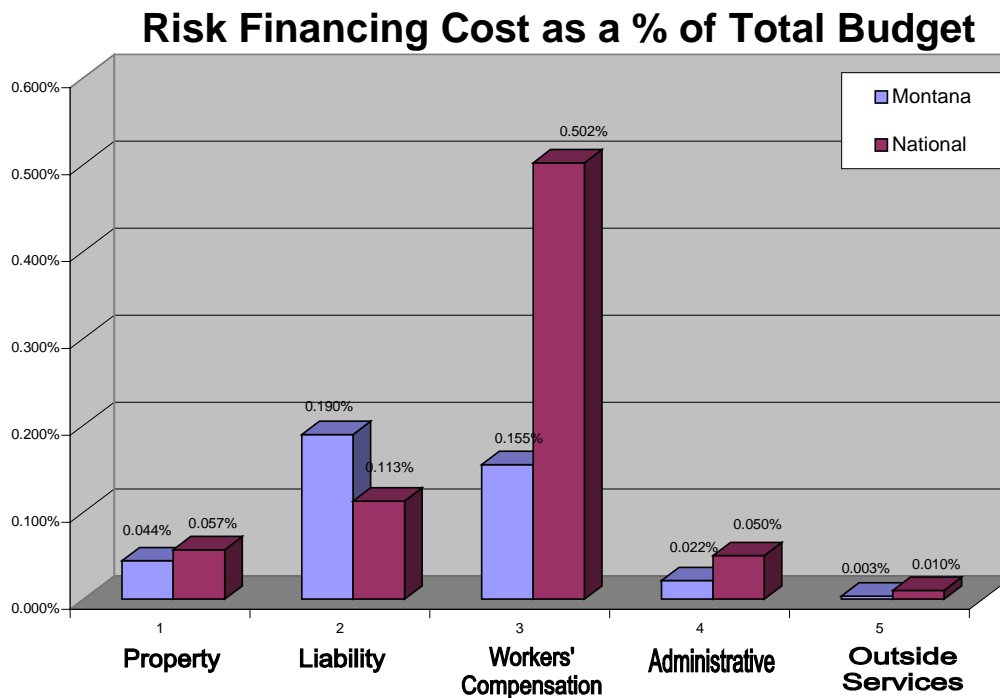


Montana spends 37% of its cost of risk dollar on workers' compensation while other governmental entities spend 71%. Although Montana decreased the workers' compensation portion of the cost of risk dollar from 46% to 37% from 1999 to 2000, other government entities increased from 45% to 71% in the same period, therefore Montana is not following the trend. Montana spends 15% more on liability and 7% more on property than its cohorts.

Montana spends less than 1% of their cost of risk dollar on outside services and 5% on administration, which is consistent with other government respondents.

### Risk Financing vs. Total Budget

The bar graph below compares the risk financing cost as a percentage of the total State of Montana operating budget to other government entities. The graph shows that Montana spent less of their total budget on cost of risk exposures in all categories except liability. Montana's risk cost as a percentage of the entire state budget, including the university system, is only 0.414%, down from 0.420% in 1999. Nationally, government agencies are using 0.823% of their operating budgets on the cost of risk.



### Deductibles and Retention

This section of the report refers to tables from the survey showing various deductibles and retention amounts for exposures by revenue size or operating budget. These tables combine all industry types included in the survey. Copies of each of these tables are included at the end of the report.

Montana's operating budget in FY2000, including the university system, was approximately \$3.5 billion. This puts us in the revenue size/operating budget category of \$2.5 - \$5.0 billion for each table.

Table 16 shows liability deductibles/retention carried. Montana does not have a liability deductible as this exposure is entirely self-insured. The retention carried would be \$1.5 million as set by statute. This retention puts Montana in the 16% category on the chart. Only 16%, or 13 of the 81 respondents had liability retention this high. 25% had retention of \$501,000 to \$1,000,000, while 20% had retention of \$101,000 to \$250,000. More respondents had a lower retention than in 1999. Keep in mind that some respondents may purchase commercial insurance to cover themselves to higher limits.

Table 19 shows the property deductible carried by size of operating budget. Montana has a \$150,000 property deductible for all entities except the prison, which has a \$250,000 deductible. This deductible is the amount RMTD pays before commercial carriers participate in the loss. This puts us in the \$101,000 to \$250,000 range. 11%, or 9 respondents share this category. The most common deductible range is \$51,000 to \$100,000 with 23% of the respondents.

Risk Management and Tort Defense had 13 FTEs in 2000. The average number of FTEs in RMTD's budget range was 14.2. This is shown in Table 21 included with this narrative.

### Summary

As with any study, one has to be careful in drawing conclusions and recognize the limitations of the underlying data. The survey is based on questionnaire information presented to a variety of different entities. Each of these entities uses different data gathering techniques and assumptions, as well as having different operating objectives. The survey, however, is the best source of information currently available from which to draw conclusions. This years questionnaire received more responses from large entities with more that \$10 billion in revenues, which contributed to a decrease in the national cost of risk for all respondents. This group, which accounted for around 50% of total respondent revenues this year has a very significant influence on weighted average results because of their extremely large size. While the overall weighted average cost of risk dropped, the median cost of risk increased from last year's survey for all respondents.

Montana's total cost of risk has continued it's declining pattern, primarily due to the reduction in workers' compensation costs. In FY2000, we spent more of our cost of risk dollar on liability costs than the survey shows other governmental entities spend, and spent significantly less of our dollar on workers' compensation exposures.

In terms of the amount spent on exposures as a percentage of the total budget, Montana spent less than the other governmental entities in the survey in every category measured except liability. Overall, however, Montana spent less of the total operating budget than their counterparts.